May 1991 Monthly Survey

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Surveys of Consumers

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SLOWER PACE OF RECOVERY EXPECTED
LAGGING INCOMES CURTAIL ABILITY TO BUY

Index Slips

The Index of Consumer Sentiment slipped to 78.3 in the May 1991 survey, from 81.8 one month earlier and 87.7 in March. While the March surge and the April retreat certainly resulted from the fleeting impact of euphoria, the continued May sag suggests a growing recognition among consumers that the road to full recovery will be long and the pace of improvement slow.

The May decline reflected a diminished outlook for the pace of the economic recovery during the year ahead. Lagging incomes continue to limit consumers' ability to buy, resulting in the weakening buying attitudes toward large household durables and vehicles, while home buying conditions improved slightly, supported by lower mortgage rates.

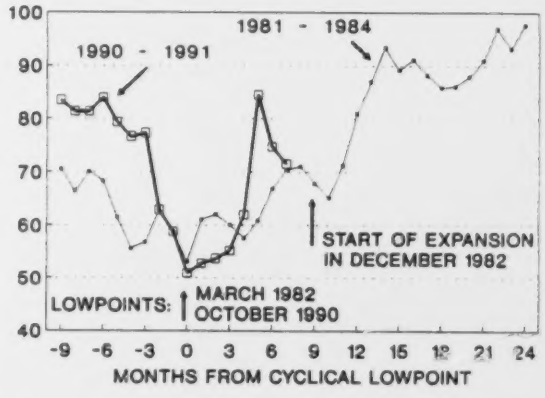
The largest declines in the Index of Consumer Sentiment were recorded among residents of the Midwest (76.6 in May, down from 85.2 in April), followed by the Northeast (73.5, down from 78.8). In contrast, very little change was recorded among residents of the Southern region (79.0 in May, from 79.9 in April), or in the West (84.0 in May, from 83.5 in April).

Leading Indicator

The Index of Consumer Expectations fell to 71.5 in the May 1991 survey, from 74.7 one month earlier and 84.5 in March. The recent losses amount to about half of the post-war surge, leaving the Expectations Index still well above the 62.0 recorded in February 1991 and the October 1990 low of 50.9.

Despite the evaporation of the initial euphoria, the Expectations Index remains on an upward trend, at a pace comparable to the rate of improvement recorded prior to the start of the last recovery. As shown in the chart below, the Expectations Index reached a low nine months prior to the start of the last expansion. Overall, the recent trends remain consistent with the start of a recovery during the third quarter of 1991.

Index of Consumer Expectations



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Slower Pace of Improvement Expected

Consumers continued to view the economy in recession in the May 1991 survey by a wide margin. Among all families, 72 percent thought that the national economy had worsened during the past year.

Despite this widespread view of the current state of the economy, consumers were more likely to expect the economy to improve rather than worsen during the year ahead by more than a two-to-one margin in the May 1991 survey. This represents a substantial turnaround from last Fall, with the proportion that now expect the economy to improve more than tripled the September 1990 low.

It has not been that consumers have changed their view during the past few months that the economy would improve, but they have revised downward the rate and extent of that expected improvement. Just 34 percent of all households in the May survey expected the reestablishment of good times financially in the economy during the year ahead, down from 40 percent in April and 48 percent in March. Despite these declines, the overall trend is still tracking upward, with nearly three times as many households expecting good times financially in the economy as a whole in May as at the end of 1990.

Unemployment Expected Persist at High Levels

Concerns that the national unemployment rate will remain at high levels during the year ahead continued to be expressed by the majority of consumers. Most consumers in the May 1991 survey expected the national unemployment rate to either remain at it current high level (44 percent) or to increase further during the year ahead (43 percent). Just 12 percent expected the unemployment rate to decline during the year ahead.

The recent trends in unemployment expectations indicate a movement toward the view that unemployment is nearing its cyclical peak, but not that it will soon decline. Indeed, throughout 1990 and thus far in 1991, there has been little change in the proportion of families that expected declines in the national unemployment rate. Rather, the change has been focused on the extent of expected increases in unemployment.

During the last half of 1990, the proportion of households that expected increases in unemployment rose rapidly (from 37 percent in July to 60 percent in December), while the proportion that expected an unchanged rate fell (from 54 percent in July to 34 percent in December). Thus far in 1991, the reverse has been true: those expecting further increases has fallen substantially (from 62 percent in January to 43 percent in May), while the proportion that expected no change in the unemployment rate rose (to 44 from 29 percent).

Inflation Expectations

Consumers expected an annual inflation rate of 4.6% in May 1991, up slightly from the three-year low of 4.3% recorded in April. Following repeated declines from the high of 6.1% recorded nine months ago, inflation expectations appear to have stabilized at levels comparable to those recorded prior to the Persian Gulf crisis.

Interest Rate Outlook Improves

In the May 1991 survey, as many consumers expected interest rates to decline as increase during the year ahead (33 percent). This represented a small improvement over the month earlier reading, although it was insufficient to regain all of the ground lost since the start of the year when 42 percent expected declines. Overall, interest rate expectations were much more favorable in May 1991 than last Fall or Spring, when approximately five times as many families expected increases as decreases.

Personal Finances Strained By Lagging Incomes

Consumers' evaluations of their personal financial situation have showed very little change during the past nine months. Among all families in the May 1991 survey, nearly as many families reported that their financial situation had improved as worsened (36 versus 34 percent). Income declines were reported by 22 percent of all households in May 1991, unchanged from one month earlier, and substantially above the 12 percent recorded one year earlier. In addition, complaints that rising prices had reduced living standards rose to 19 percent in May 1991, after falling to a low of 14 percent at the start of the year.

Consumers view their financial prospects for the year ahead in more positive terms. Among all families in the May 1991 survey, 37 percent expected their financial situation to improve during the year ahead, up from a low of 26 percent in December 1990, and the highest proportion recorded since last May. Nonetheless, consumers' reports of the expected size of the increase in household incomes were very small, indicating that the overall improvement they anticipated for the year ahead in their financial situation will be marginal.

Household Durables Purchases Limited by Lagging Incomes

The May 1991 survey recorded declines in the proportion of families that held favorable attitudes toward buying conditions for furniture, appliances, and home electronic goods. Among all families, 61 percent voiced favorable attitudes in the May survey toward buying conditions for large household durables, down from 67 percent one month earlier and 63 percent two months earlier. Although the proportion holding favorable buying attitudes toward large household durables was above the low of 53 percent recorded at the start of the year, they remained well below the year earlier reading of 75 percent.

Despite the fact that references to price discounts on household durables remained frequent, it was consumer references to their ability to buy, not market prices that led to their more cautious spending views.

Prospects for Home Sales Brighten

Attitudes toward buying conditions for homes were more favorable in the May 1991 survey than any time during the past year. Among all families, 74 percent thought home buying conditions were favorable in May, up sharply from the October 1990 low of 50 percent. Most of the improvement, however, was recorded from October 1990 to March 1991, with little further change since then.

The improving trend has been due to more favorable perceptions of home prices as well as lower mortgage interest rates. Lower home prices were mentioned by 49 percent of all families in the May 1991 survey, tieing the all-time record first set in March of 1991. In comparison, just 9 percent registered complaints about high or rising home prices.

Lower mortgage interest rates were mentioned by 40 percent of all families in the May 1991 survey, just below the 43 percent recorded in the prior two months, but substantially above the October 1990 low of 11 percent.

Vehicle Buying On Hold: Waiting for Discounts

Following rapid gains at the start of the year, favorable vehicle buying attitudes have slipped during the past two months. The recent sag has been due to the continued absence of the type of deep discounting that is widely anticipated by consumers, as well as to stubbornly high interest rates on vehicle loans. Given that lagging incomes has limited consumers ability to buy, it has been these price and interest rate concerns that have been decisive in consumers' judgements of the affordability of these purchases.

The proportion holding favorable attitudes toward buying conditions for vehicles fell to 61 percent in the May 1991 survey, from 63 percent one month earlier and 66 percent two months ago. This small decline only partially reversed the rapid gains recorded at the start of the year, when favorable vehicle buying attitudes rose from 47 percent in December 1990 to 66 percent in March 1991.

The small recent loss, as well as much of the remaining strength in vehicle buying attitudes is contingent on the availability of price discounts. Among all families in the May 1991 survey, 46 percent mentioned that they expected the availability of deep price discounts during the year ahead, down from the all-time peak of 51 percent recorded one month earlier. Thus far, however, consumers see few signs of the return of substantial discounts. Indeed, the proportion of families that referred to high vehicle prices rose to 19 percent in May 1991 from a low of 14 percent three months earlier.

In sharp contrast to mortgage interest rates, interest rates on vehicle loans have not shown comparable declines. Among all families in the May 1991 survey, 16 percent mentioned lower interest rates on vehicle loans, only marginally higher than the 12 percent recorded both one month and one year earlier. Federal Reserve Board data indicate that the interest rates charged on new vehicle loans by finance companies actually increased to 13.2% in the first quarter of 1991 from 12.7% in the first quarter of 1990, while interest rates charged by commercial banks on new vehicle loans declined marginally to 11.6% in the first quarter of 1991 from 11.8% a year earlier.

Buy American--Except When Import Prices are Lower or Quality Better

The Persian Gulf war has had no overall impact on consumers' predisposition to buy products made in this country. The May 1991 survey repeated questions originally asked in 1981 about consumers' preferences to purchase products made in this country rather than products made in another country.

At the most general level--without reference to product prices or quality--it should be no surprise that most American consumers voiced a distinct preference for domestic-made products. Among all families, 60 percent indicated a general preference to buy domestic products in the 1991 survey, insignificantly above the 58 percent recorded in 1981 (see the table below). Very few consumers in either survey voiced a preference for products made in another country (4 percent in both 1991 and 1981). About a third of all families in both years replied that they had no overall preference, with their purchase depending on the type of product and price and quality differences.

Buying Preferences for Domestic Versus Foreign-Made Products

Preference for Products made in:	1981	1991
This country	58%	60%
Another country	4%	4%
No difference	38%	36%
Total	100%	100%

The vast majority of consumers that indicated a preference for products made in this country explained their views by references to patriotic motives in both years. Helping the domestic economy was seen as the primary reason to buy domestic goods.

Price and quality considerations were more frequently mentioned by respondents that were indifferent to the country in which the products were made or indicated a preference for imported products. Interestingly, the 1991 data indicated more frequent mentions of quality compared with price considerations among these respondents than was true in 1981.

Reasons Given for Country Preferences

	Preference for Products made in:					
	This Country		Another Country		No Difference; Depends	
Reasons	1981	1991	1981	1991	1981	1991
Patriotic	91%	93%	--	--	--	--
Cost	16%	3%	82%	48%	27%	32%
Quality	17%	22%	25%	71%	41%	51%
Type of Product	--	--	--	--	20%	16%

Note: Columns may add to more than 100% because of multiple mentions.

Consumers that indicated an overall preference for products made in this country were asked if they would alter their buying preferences if prices and product quality differed between domestic and foreign-made products. Of the 60 percent that initially favored buying domestic products, less than half would still favor buying domestic products if they were priced higher than similar foreign-made products. Consumers were even more responsive to quality considerations: the initial 60 percent was reduced to just 17 percent that would buy domestic made products regardless of quality differences.

Combining price and quality considerations, the initial appeal of domestic-made products was reduced from 60 percent to just 14 percent of all households. These results were nearly identical for both the 1981 and 1991 surveys.

As a consequence, the majority preference for domestic-made products only holds when product price and quality are similar. When foreign-made products cost less or have better quality, social principle yields to economic self-interest.

Consumer Reactions to Price And Quality Differences

	1981	1991
Percent Preferring Product Made in this Country	58%	60%
Reactions to Price Differences		
Buy domestic regardless of price	26%	28%
Buy foreign if price lower	27%	29%
Depends	5%	3%
Reactions to Quality Differences		
Buy domestic regardless of quality	17%	17%
Buy foreign if quality better	37%	38%
Depends	4%	5%
Reactions to Price and Quality		
Buy domestic regardless or price or quality	14%	14%
Buy foreign if price lower or quality higher	40%	41%
Depends	4%	5%

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The May 1991 survey included 500 completed interviews conducted between May 1st and May 29, 1991.